DOW THEORY LETTERS INC.

RICHARD RUSSELL
P.O. Box 1759
La Jolla, Calif. 92037

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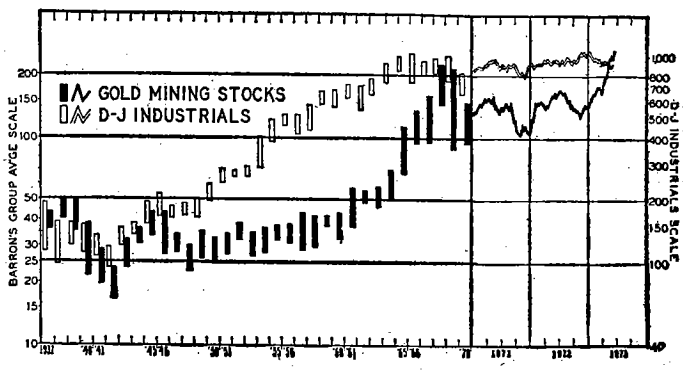
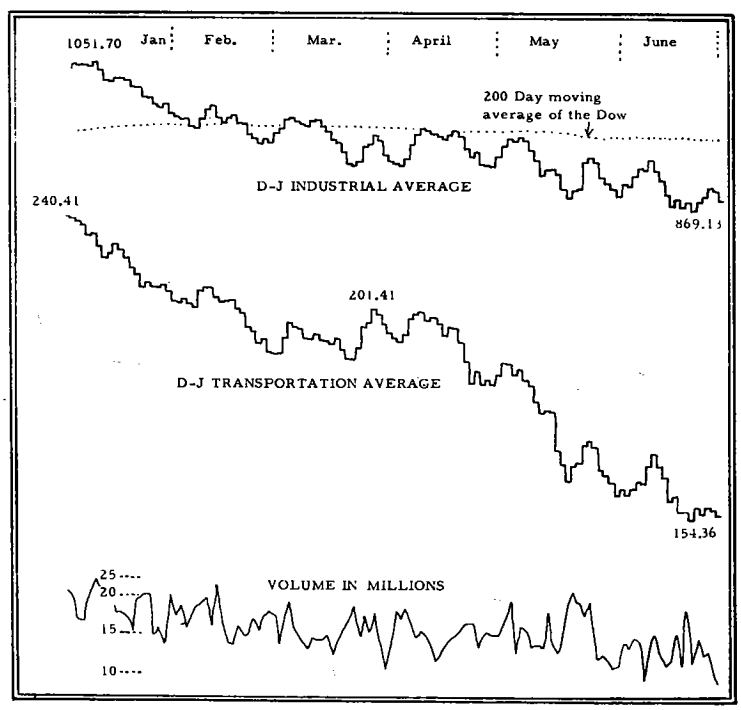
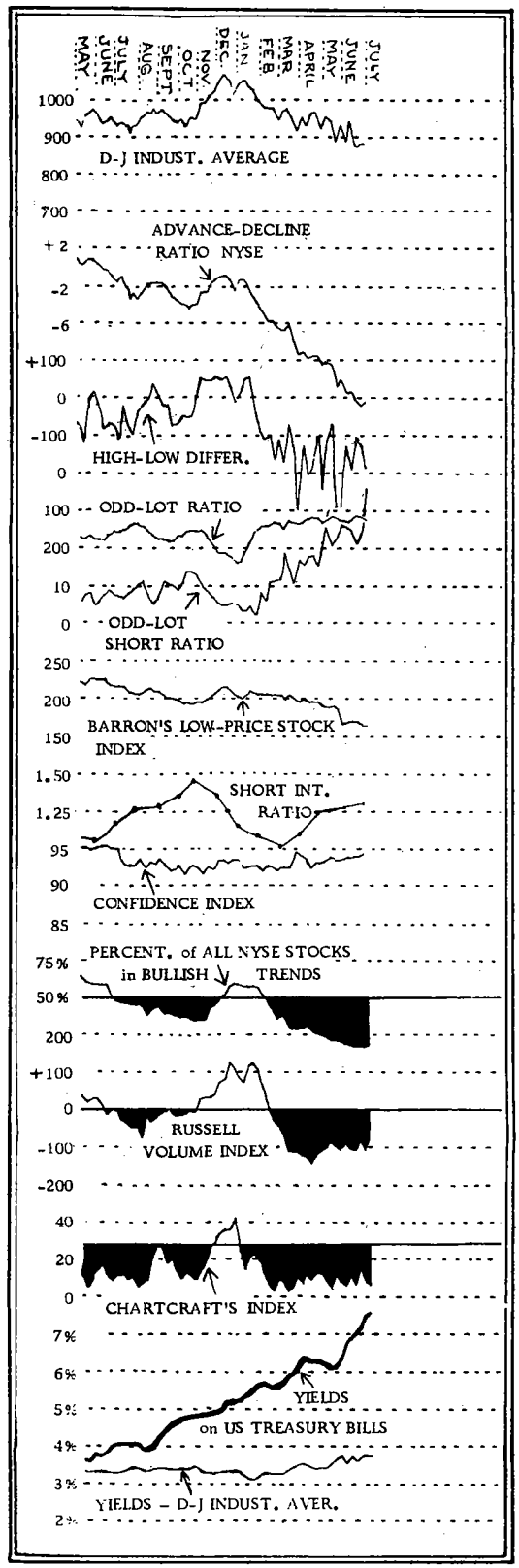
"YOU'LL FIND OUT" DEPT. A Gallup poll has just disclosed that over half (55%) of all Americans have never heard of, or had no concept of, Euromart or the European Economic Community (although the EEC now exports more goods than the US). The days of America's complacency, ignorance and arrogance (in my opinion) are now numbered.

CHART OF THE MONTH: A few weeks ago Barron's published a little chart, the significance of which probably escaped literally all its readers. Yet I consider this chart of historic importance. Here we see a ratio-scale chart of the Dow Industrials and Barron's Gold Group since 1937. Note that now, for the first time in 32 years, the Gold Group has risen above the price of the Dow. This means that if one had bought leading gold stocks in 1942, one would now be ahead of the man who had purchased the 30 "blue-chip" Dow stocks that same year. In my opinion, this chart is telling us more about the stock market, values, inflation and capital destruction than anything we can read today.







SIGNS: I received the latest (July) issue of Money, published by Time, Inc. This popular and widely-advertised magazine purports to provide the investing public with what they need to know in order to handle their money. The July issue contains an index for October, 1972, to June, 1973. I looked under the classification, "Gold." Entries — none. My conclusion — purchase of gold shares or coins is still a contrary opinion.

THE MARKET: One of my main endeavors over the past fifteen years has been to attempt to teach subscribers the overwhelming importance of the primary trend. I have explained (the Dow Theory principle) that the daily market movements are comparable to the ripples on the ocean, and that the monthly (intermediate) market trends can be likened to the larger waves of the ocean. But the major market force, the all-powerful primary bull or bear market trends, must be likened to the tides of the ocean. And as any beach-dweller can tell you, the tide, in due time, conquers all.

One of the things our Government leaders have never learned is that although the tide can be manipulated or temporarily held back, it cannot be reversed. All the power of all the world's presidents, kings, treasurers, congresses, and all their respective public relations flunkies cannot reverse the primary tide. The tidal force of the market, always, always runs to its inevitable conclusion. I have written that when the tide is temporarily held back or manipulated, the pressure builds up. And when that compression is finally released, the resultant force is greater, more violent and more persistent than ever.

This week, as I looked over the wreckage of the market, I could not help thinking of the massive amounts of time, effort, and money that the US Government has spent in attempting to hold back the bear market tide. Yet the year 1973 has produced one of the ghastliest market collapses that I have ever seen. A straight-line crash in the advance-decline ratio, a shattered Transport Average, a Value-Line (broad unweighted) Average which has broken its 1970 bear market low, new lows on the D-J Industrial Average for the past two years, a pulverized AMEX and a totally demoralized ("non-liquid" is the term) over-the-counter market, plus widespread margin calls to investors across the nation.

On top of this, I note that the funds have fared horribly with the average of all funds down over 20% in 1973. The May, 1973, Mutual Fund statistics shows that the funds sold $477 million of stocks on balance, a figure surpassed only by the February, 1973, sales-over-purchases figure of $563 million.

Why are the fat earnings of 1973 failing to hold this market up? Why has the market had a heart attack in the face of all the good earnings news? My only answer is that Wall Street knows all about the earnings and is obviously preoccupied with something else. Could that something else be the rotting of capital and savings via inflation? Is the average American finally facing the possibility that he is running up the down-escalator of inflation? "Inflation," it has been said, "is bullish up to a point. Beyond that point it becomes synonymous with destruction." Does the average citizen know that the point of no return is passed? I think he does. He now knows that continuing inflation can only bring more controls, more problems, more disintegration of capital and savings, more official robbing of Peter to attempt to pay Paul.

On the Wall Street front, many market analysts are discovering what I have been warning about — bear markets don't work like bull markets! This generation of Wall Street "experts" has been weaned on the bull market era of the 1950's and early '60's. Then the market went up, corrected, and repeatedly rose to new highs. Ultimately, the bull tide bailed everyone out of their mistakes and bad guesses. But today we have an animal of a different color. This bear market is not going to bail anyone out. It's going to sink them, and so far in 1973 the bear has been doing an excellent job of ripping, rending and clawing.

The fact is that even the pessimists have been astounded as "oversold" areas have been smashed, "support levels" have evaporated, and "buy signals" have been blown away like fluff in the eye of the storm. Perhaps most disconcerting (except for the price declines themselves) has been the low volume during 1973. But rather than signify "a lack of selling pressure," the low volume has simply locked in vast amounts of stock at higher prices. In a primary bear market, when the market sinks on low volume it means that stock values are evaporating but nobody is getting out. "Where does the money go when a stock drops?" is a question I have been asked. It doesn't "go" or transfer anywhere, is the answer. It is lost. Perhaps I can illustrate it in this way: Where does the value go when someone drops a rare jewel and it shatters? The value simply disappears, and that unfortunately, is exactly what happens to stock values.

In the opening section of this Letter I described the Dow Theory principle of the three market movements (daily, intermediate, primary). It is also essential to understand the Dow Theory concept of the three phases. These phases occur in both bull and bear markets (I will confine my discussion to bear markets at this time, since that is what we are currently concerned with).

The phases refer only to the psychological areas, not price movements. Coincidentally, however, the phases are often separated by upward correction in the price movement (downward corrections during bull markets). The first bear phase represents the initial collapse from the previous speculative bull market top. Thus, we had the 1966 cave-in from the frothy 1965-66 bull peak. That phase ended in October, 1966, at 744.32, following a drop of 264 Dow points.

The second phase began in late 1966, and it is still in effect. The second phase of a bear market is the one in which the market reflects continuing deterioration in the social, political or economic background for corporate shares (often all three). At some point in the second phase the market goes down simultaneously with business, as the bad news surfaces and as the corporate picture turns from gray to black. Historically, the second bear market phase is the deceptive one, and we are currently wrestling with what I consider the most deceptive bear market second phase in history. By definition, prices at the conclusion of the second phase are below prices at the termination of the first phase. If that comes to pass, this second phase will end with the Dow at new lows for the entire 1966-73 period or below the 631.16 low of 1970.

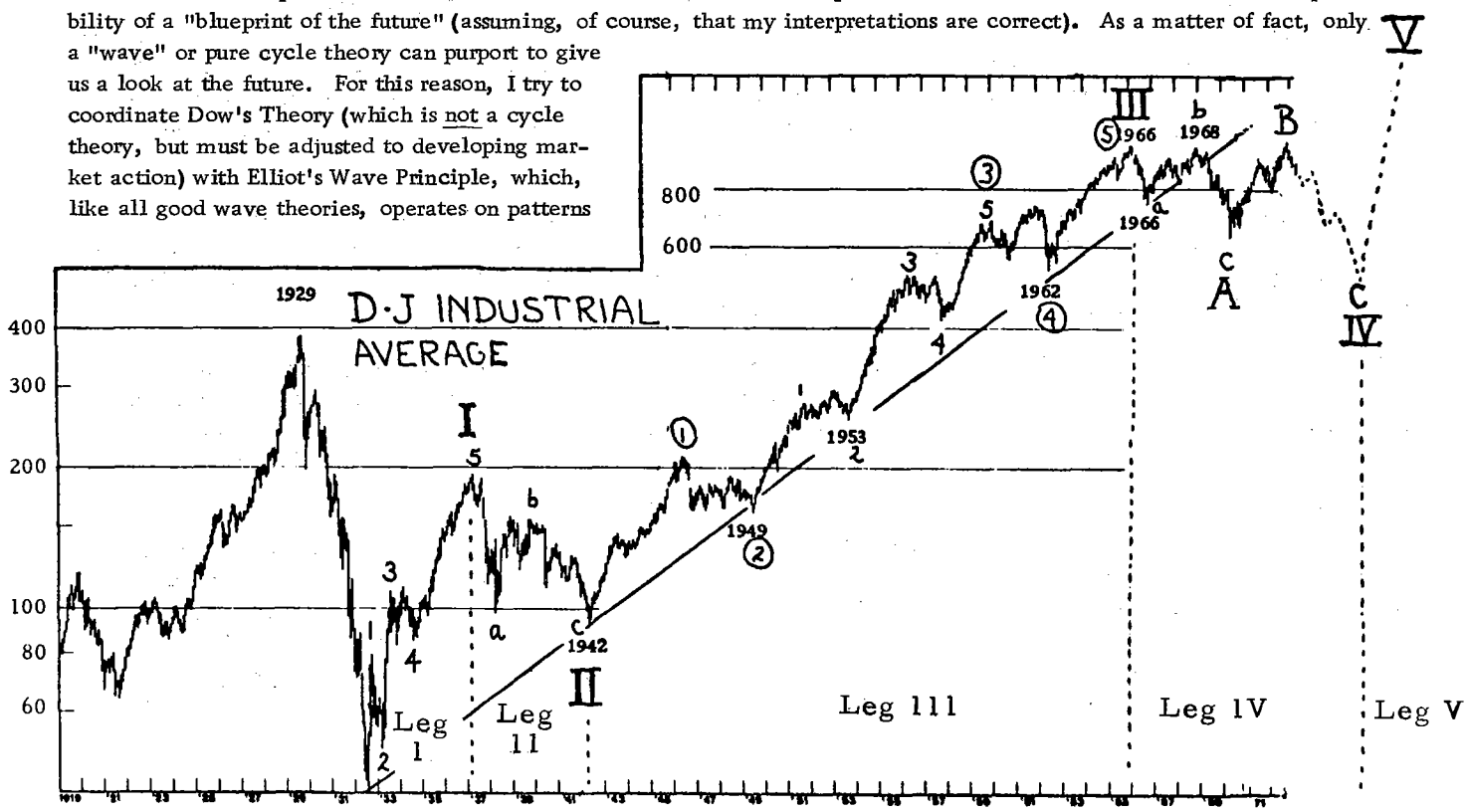
The third phase of a bear market (we are not there yet) is the one in which stocks are sold because people need the money to live on, to do business with or to pay bills with. This is the liquidation phase, and here stocks go below known values. The slogan during the third phase could be, "Don't bother me with what it is worth, just tell me whether there's still a market for it!"

In the last Letter I opined that a rally or upward correction could be nearing. In reading dozens of other investment services this week, I get that "crowded-in" feeling that most of the advisories are also expecting a nearby recovery advance. It is also true that my Primary Trend Index (PTI) is crashing steadily into new ground, and the Utility Average (a good leading indicator) is melting to its lowest level since 1970. And as a sort of coup de grace, bellwether IBM today cracked 300, thereby plunging to a new low for the year (could this signal a general collapse in the high-multiple institutional "pin-up girls"?). My two most-active stocks indices (see last report) both look bad, very bad, and this too, casts a pall over this low-volume, slowly expiring market.

Two positives for Wall Street (from my standpoint) are (1) The market has been in a state of collapse during all of 1973, but every point down is a point nearer the bottom (and the averages are not going to zero this year), (2) "Will-Go" (see Letter 563) calls for some upside (remember that word) action around the first week in July.

My conclusion is that subscribers who have followed my endlessly repeated advice to buy gold shares (by the way, I follow my own advice) are not sweating out the collapse or the inevitable rally. Prices for gold shares are at or through the roof and golds are now going up "on their own" (not against the market in the old, contra-cyclical manner). Readers of these reports are playing for the approximate long-term gold top and the approximate long-term market bottom. My studies show that we are nowhere near either, regardless of the market's "ripples or waves."

ELLIOT'S WAVES: Everyone would love a real "peek into the future," and this is a particular fantasy of stock market students, investors and economists. I tried to provide such a peek in Letter 562, which offered a lengthy discussion of Elliot's Wave Principle. One of the fascinations which the Wave Principle holds for me is that it offers at least the possibility of a "blueprint of the future" (assuming, of course, that my interpretations are correct). As a matter of fact, only a "wave" or pure cycle theory can purport to give us a look at the future. For this reason, I try to coordinate Dow's Theory (which is not a cycle theory, but must be adjusted to developing market action) with Elliot's Wave Principle, which, like all good wave theories, operates on patterns



 which are "preordained" and are in harmony with "nature's law of motion." Perhaps because some of my Elliot comments (from Letter 562) have been coming true, I have received many Letters asking me to update the market picture. Here, then, is an updating of Letter 562.

I cannot repeat all of the basic Elliot Wave Principles set forth in Letter 562 (new readers may purchase xeroxed copies of Letter 562 for $4.00 plus a self-addressed envelope), but again I ask all subscribers to save and file each of these reports so that they can be used for future reference. Mr. A.J. Frost of Canada is probably the greatest living interpreter of Elliot's Wave Theory. Mr. Frost worked with the great Hamilton Bolton (founder of the Bank Credit Analyst), and some of Frost's outstanding Elliot analyses have appeared in the Analyst. I have had some correspondence with Mr. Frost recently, and needless to say I am always intensely interested in what he has to say about Elliot.

Elliot interpretations of the market require much work, knowledge and artistry. Mr. Frost keeps a good many charts varying from long-range graphs to actual hourly chart of the Dow. It should be born in mind, however, that Elliot is basically a method for making "sense" out of the market movements, much as an oceanographer might attempt to make sense out of the patterns of the tides.

Elliot students must constantly check, recheck and even change their data and interpretations as the movements of the market unfold. Mr. Frost has at least two possible long-range interpretations of the market, one theorizing that a major bull cycle began in the early 1800's leading to a peak in 1916, a correction (leg 4) to 1942, and then a series of 3 legs to 1966. Under this way of thinking, we are now in corrective leg 4 which should end perhaps in 1976, prior to a final leg 5 which might end in the early 1980's while perhaps taking the Dow to 2000 or better.

The second Elliot thesis is the one that I personally feel more "at home with." I have drawn a chart which serves to illustrate the second interpretation. This Elliot thesis states that a supercycle began in 1932. The supercycle was to take the form of five typical but major Elliot waves, three up and two (corrective waves) down. I have labeled these five major legs on the chart with Roman numerals. As we can see, three of the legs are already completed, and we are now in the midst of major Elliot wave IV (which is a corrective or bear market leg, as was major leg II). Chart on page 3.

Now let's examine the major Elliot legs. Leg 1, the first upward leg, carried the Dow from the Great Depression low of 41 to the 1937 bull market peak of 194 (Roman numeral I on chart). Leg 1 (which was composed of 5 smaller legs, 3 up and 2 down), was followed by a major but typical 3-leg correction. This is shown on the chart by Roman numeral II, and it carried the Dow down to the 1942 low of 92.

Major Elliot leg III is identified by the Roman numeral III on the chart. This was an extremely complex leg, containing many smaller bull and bear markets. I have broken leg III down on the chart so that readers may study it. This is the enormous upward leg which contained not only the 1942-46 bull market but the great 1949-66 bull market. Leg III was born during 1942 (in the depths of World War II) with the Dow at 92. It ended 24 years later in the midst of the booming 1960's (1966 to be exact) with the Dow at 995. From there Elliot leg IV began, and this was to be the second major correction of the whole Elliot Supercycle since 1932 (the first correction, of course, being the 1937-42 collapse or leg II as seen on the chart).

So much for history. The important thing is: what is occurring now and how does it fit into the Elliot picture? The current major Elliot wave IV is taking the form of an A-B-C "flat" type correction. In flats, the B peak often approaches or betters the preceding peak or the peak from which the whole correction begins. Thus, the 1972 Dow peak (B on chart) of 1051.70 bettered the 1966 peak of 995.15 (995.15 being the point from which the entire Elliot leg IV started).

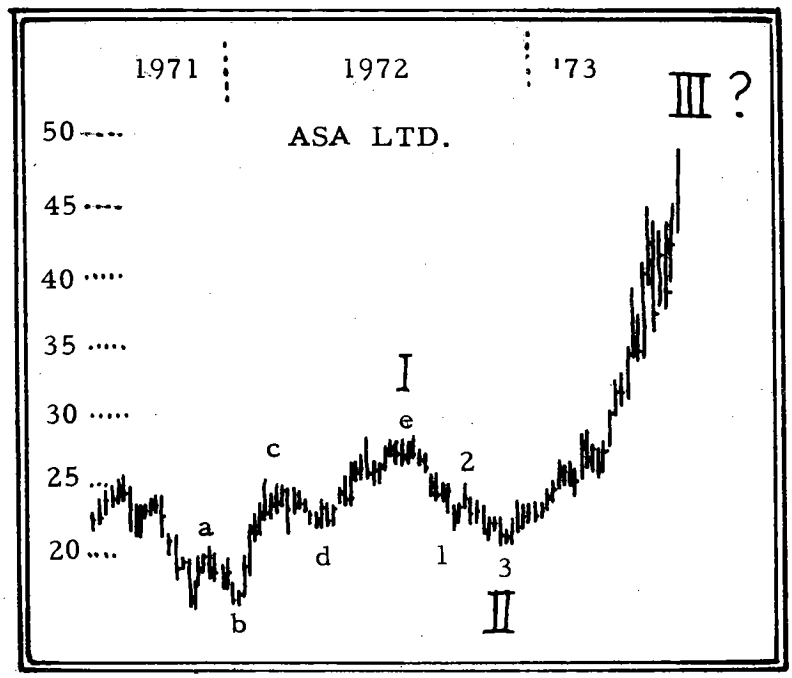
It is well to remember that regardless of whether we follow Frost's first interpretation or his second (I prefer the second which is that the bull market began in 1932), we are nevertheless currently in a leg IV Elliot bear market correction. Furthermore, we are now in the third or final (C) leg of the major A-B-C bear market as seen on the chart. Note that the current leg IV Elliot bear market correction has cracked the entire 37-year upward trendline, a trendline which has held since 1932. This is typical of major Elliot corrections, and it demonstrates the seriousness of the current descent.

The fact that we are now in an Elliot leg IV correction provides one interesting guideline, and one that I hope we never have to use! In Elliot bear markets, most leg IV declines hold above the peak of leg I, as discussed in Letter 562. Since the peak of leg I was the 194 peak of 1937, no decline from here should break 194 on the Dow (is that a consolation?). At any rate, my own guess is that the 520 peak of 1956-57 should act as a very strong downside resistant level for the Dow. Frost writes that "C" waves tend to be exponential, however, and I have often been fooled by the power of a C wave (both of the bullish and bearish variety). Thus, if the 520 area is ever broken on the downside, it would (I feel) be an omen of utter disaster.

What of "future leg" V as outlined on the chart via the dotted line? This would be a major primary bull market and one which would finish off the whole supercycle since 1932. Such a bull market could be fueled by a drastic change in the money equation, either (1) a great rise in the gold price and a major period of high prosperity, or (2) a 1975-76 depression, with a subsequent massive inflation as the world attempts to print itself out of the doldrums.

But perhaps it is too early to speculate about leg V and its possible cause and effect. Let's see how "intuitive" the Elliot observations are for the development and final completion of current leg IV. (And another thanks to Mr. A.J. Frost for his help and thoughts on the whole question of the Elliot Wave Principle).

ELLIOT AND GOLD: Following the last Elliot study, I received many Letters asking if I would apply the Wave Principle to the gold shares. All the listed golds are in roughly the same pattern, and I have chosen ASA Ltd. for purposes of Wave study.



The accompanying chart shows the action of ASA from mid-1971 to date, on a weekly basis and drawn to arithmetic scale. As I interpret Elliot, we are now in a major primary bull market in gold shares. The bull market began for most South African gold shares in 1971, and this is where I am placing the start of the bull market in ASA.

The first major upward wave of what should be a five wave bull market (3 waves up, 2 corrective waves down) began in late-1971 as shown on the chart. Wave 1 carried to mid-1972 and took the form of 5 typical smaller waves (marked a through e). Next, we had the classic 3-leg corrective wave which shows on the chart as Roman numeral II.

From late-1972, we went into major wave III, and this should assume the form of a 5-leg rise. Wave III (so far) is very unusual because so far there is little evidence of correction, and at least two corrections should appear before leg III is finally completed (the first important decline in ASA could constitute the first correction of wave III).

As I see it, wave III in ASA should turn out to be a whopper on the upside. It should be followed by a correction (wave IV), and then a final leg V up. In other words, under my Elliot interpretation ASA (and therefore all the golds) have a long way to go on the upside before the bull market in the gold shares is over.

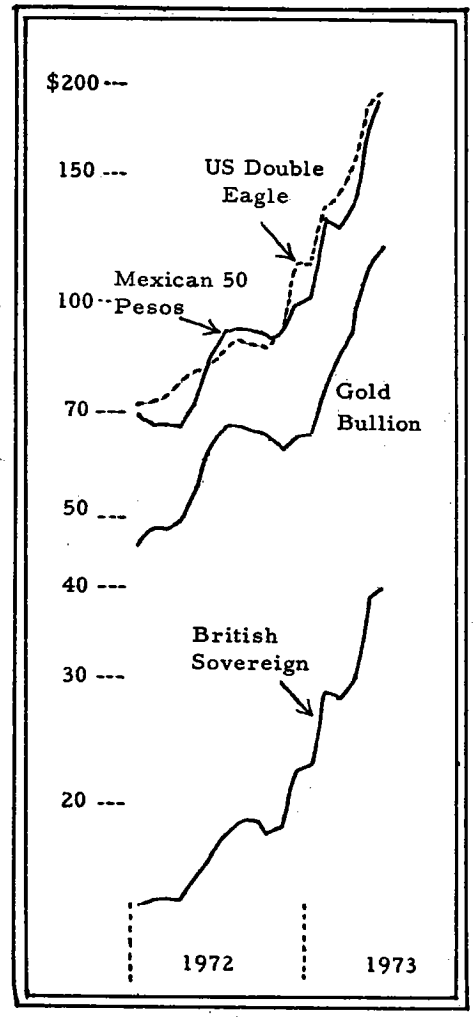
One rather important piece of evidence has been building, and I have not seen this information anywhere else. Veteran market students know what happens when a short position builds during a primary bull market. The rising short position indicates that too much bearish sentiment is accumulating against the primary trend. Ultimately, this bearish sentiment is driven out, and the shorts are forced to run for cover as the market roars higher.

There is an obvious primary bull market now in force in the gold shares. The figures below cover the short position (figures in thousands) in the four listed NYSE gold stocks.

	March	April	May	June
ASA Ltd.	11	14	7	23
Campbell	12	19	12	13
Dome	14	0	0	11
Homestake	24	30	28	31
TOTALS	61	63	47	78

If these figures continue to build, the ultimate resolution should be a virtual explosion in the price of the gold shares as the gold bears find they are fighting a primary bull trend and are consequently driven (literally) "to cover."

GOLD (cont'): I have written about gold coins briefly before, suggesting that they could be profitable speculation. That was when "double eagles" (containing one ounce of .900 fineness gold) were selling under $80 per coin. The typical double eagle now sells for above $190 retail. The question, what are the advantages of gold coins? First, a gold coin represents an investment in intrinsic value. You can hold a coin in your hand, you can take it anywhere, you can bury it in your backyard, you do not have to sell it through a stock exchange. Gold mines become depleted, they can burn or flood, they can be struck. Gold coins throughout history have done two things, they have (like gold) held their value or gone up in value.



If you hold a gold coin for six months or more, you can declare any profits of the sale as a capital gain. Yet, gold coins are not officially classified as securities. Therefore, they do not have to be registered or recorded. They are "anonymous." You can invest in "common" US gold coins (the "meat and potatoes" of the coin world),you can buy rare coins, foreign coins, you can buy coins for cash or on margin.

I obviously do not have space to go into all the ramifications of gold coins, but I do want to say that there are a number of interesting gold coin investments such as the Mexican gold pesos, the British gold sovereigns, the US "eagles," etc. Any competent coin dealer should be able to get you information. One factor should be noted, however. Gold coins command various premiums over their gold content. Most of the common gold coins command less than a 100% premium over their actual gold value. The rarer gold coins command a greater than 100% premium.

Do gold coins hold their premium over the gold price during a rise in the gold price? Here I am including a gold chart I have drawn showing what happened during 1972 to date as gold bullion climbed from roughly $46 an ounce to $120 an ounce (June, 1973). I have traced the average price path of the typical British sovereign containing .23 oz. of gold .916 fine (91.6% fine), the Mexican 50 peso which is 1.2 oz. of gold .900 fine, and the US "double eagle" which contains .96 oz. of gold .900 fine. All coin prices are drawn to ratio scale so that exact percentage of movement can be compared, regardless of price level.

The chart shows that they have all pretty much kept pace with the rise in gold. Will they continue to hold their premium (the price premium above their actual gold content)? Probably, but no one can know for certain. Would these coins hold their premium over gold if ownership of gold was legalized in the US? Again, there is no way of telling, but I would think that with the rising interest in the gold coin (which is a "vanishing species"), gold coins will tend to hold their premiums. However, if gold ownership is legalized in the US, my feeling is that millions of people would rush in (as the Japanese have) to buy gold as an inflation hedge, and the price of gold and gold coins would move substantially higher. Therefore, legalization of gold in the US might have the affect of narrowing the gold coin premium over actual coin gold value, but the rising price of gold would more than make up the difference in overall price.

One thing to consider is that US coins do command a premium over most other modern gold coins, perhaps because of sentimental value. The same seems to hold true of US stamps. This could conceivably change some time in the future, but for now there is a certain "collector's extra" in the fact that the gold coin is a US issue. In closing this section, I again repeat that there is no substitute in the coin field for an intelligent, competent, honest dealer.

LATE NOTES: In the last Letter I wrote that this report would be mailed on July 11. Well, I thought too much was happening so — I am sending this Letter out earlier than expected.

A good deal is being written now about the US's slowly improving trade position. This is due, in large part, to the collapse in the dollar's value and the fact that US goods are looking "cheap" in terms of foreign currencies. Problem: in terms of dollars foreign goods are getting expensive. Watch for a drop-off in foreign sales to the US. Trade and export problems on the part of Europe and Japan are emerging. Result — coming retaliations by our overseas competitors. International trade is like Watergate, when the chips are down it's "every man for himself." And the chips, in case you missed it, are down!